

ST 13-0002-PLR 07/31/2013 CONSTRUCTION CONTRACTORS

When a construction contractor permanently affixes tangible personal property to real property, the contractor is deemed the end user of that tangible personal property. As the end user, the contractor incurs Use Tax on the cost price of that tangible personal property. See 86 Ill. Adm. Code 130.2075. (This is a PLR).

July 31, 2013

Dear:

This letter is in response to your letter dated May 31, 2012 in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) to review regulations, letter rulings and other types of information relevant to your inquiry.

Review of your request disclosed that all the information described in paragraphs 1 through 8 of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling, and is subject to the provisions of subsection (e) of Section 1200.110 governing expiration of Private Letter Rulings. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request. In your letter you have stated and made inquiry as follows:

We are writing to request a Private Letter Ruling regarding our interpretation of the taxability of the outlined transaction.

The taxpayer has undergone a recent audit that is now closed. A similar transaction was included in the audit period. The auditor stated that the taxpayer should be treated as a construction contractor since the materials were incorporated into real property. The Department, however, decided not to follow this treatment before the audit was closed. The auditor indicated that future transactions similar in nature would be treated as being incorporated into real property and the taxpayer would be treated as a construction contractor.

We have found conflicting information between the auditor's stated position and other supporting documents. For this reason, we request the Illinois Department of Revenue to review the outlined transaction and respond to the stated tax determination.

**QUESTION**

Is the transaction subject to Retailers' Occupation Tax or Use Tax?

**FACTS**

COMPANY ("Taxpayer" or "Company") is located in STATE and has individuals working in the State of Illinois. The taxpayer sells new and used racking systems which hold bins, containers, and pallets. The company subcontracts the installation services and these services are provided under one contract (purchase order) with the customer. The taxpayer also provides warehouse design services to facilitate the most efficient placement of the racking systems. In addition, the taxpayer provides racking system removal services where an existing system is purchased from the customer. In most instances, the systems that were removed are held for resale.

The racking system is bolted to the floor via an anchor in the floor that has a threaded shaft emerging from the floor. The system is then placed on top of the threaded shaft and has a bolt securing it to the building floor. The taxpayer installs the anchor.

The systems are intended to be installed for a short period of time (typically less than 5 years). After five years, the system is typically reconfigured within the customer's location or a new system is installed.

Upon removal of a system, the threaded shaft securing the system is merely hammered into the floor. The threaded head is hammered until it is flush with the floor (required for safety precautions). The anchor is noticeable upon close inspection but it does not disrupt the surface of the floor. Also, there is no damage to the floor that requires repair.

## **STATEMENT TO SUPPORT TAXPAYER'S POSITION**

There are two underlying factors used to determine the taxpayer's position. The first is the definition of permanently affix and the second is the intent of the transaction by the parties. We have aligned both items with the facts of the transaction.

### *Permanently Affix*

As noted, the racking system is secured to the floor via a nut on a threaded shaft of an anchor (bolt). The use of an anchor with a threaded shaft is to secure the items for stability and safety.

The removal of a system does not cause any damage to the floor. As part of the removal process the threaded anchor is hammered into the floor. This does not crack the floor or weaken the structure of the floor. No concrete patch is placed over the anchor and no other repair work is required.

Illinois Private Letter Ruling No. ST 06-0002-PLR, 03/03/2006 provides that "... bolts, screwed into the anchor holes, are used to secure the material handling system to the floor. The material handling system is not permanently affixed to the realty." This installer has some varying facts and circumstances but what appear to be the pertinent issues to this determination are similar to this company.

### *Intent*

Illinois Department of Revenue General Information Letter No. ST 04-0105-GIL, 07/01/2004 indicates the department may utilize the intent of the parties to make a determination.

The intent of the buyer and seller is that the system is installed with full knowledge that it will be removed at a later date. This is evident by the multiple examples of Illinois customers where a system was installed and within a few short years the company is engaged to re-configure the warehouse, remove the old equipment and either relocate it within the warehouse or remove it and install a new system. Also the relocation and/or removal of a system is a relatively quick process that can be managed in a matter of days.

This is a typical set of facts regarding the installation and removal or relocation of a system.

It may also be important to address that the company does not retain a security interest in the product. The customers are very consistent regarding prompt payment (within 30 – 90 days). The company does not have bad debt or collection issues that would require the need for a security interest.

Lastly, the system is not customized to one customer. It is interchangeable in that two customers could use the same product. The layout may differ but the product itself can be the same.

#### **STATEMENT CONTRARY TO TAXPAYER'S POSITION**

The auditor's position that the taxpayer is a construction contractor is based upon Title 86, Part 130, Section 130.1940, ST 89-0084 – 02/01/1989, and ST 96-0198 – 05/14/1996. Our understanding of that determination is based upon the following written correspondence from the auditor:

*In instances when you sell both material and permanently affix that material to real estate, you are acting as a construction contractor. The Department views permanently affixed as bolting or anchoring into floors/real estate. Although these items can be uninstalled, it is not any easy process and damage occurs to floors and repairs have to be made. I have attached some letter rulings that reference this. Construction contractors are responsible for paying the use tax to the Department on the cost of the materials they install for the jobs as they are deemed the end user of such materials. I have attached regulation 130.1940 (see c)) regarding this. Use tax is not due if the customer that you are performing the job for gives you an exemption certificate. These are typically E# letters stating that the person is organized and operated exclusively for charitable purposes (like the letter that you provided earlier in the week). Items could also be exempt if the job was in an enterprise zone or if the customer had MPC. No other exemption is valid for these jobs.*

In addition to this, multiple General Information Letters published by the Department (i.e. ST 12-0018-GIL, 03/27/2012) indicate the following:

*A contract that provides for both the sale and installation of tangible personal property that is permanently affixed or incorporated into a structure is considered a construction contract. The tax liabilities regarding construction contractors in Illinois may be found at 86 Ill. Adm. Code 130.1940 and 130.2075 on the Department's Internet website. The term construction contractor includes general contractors, subcontractors, and specialized contractors such as landscape contractors.*

*In Illinois, construction contractors are deemed end users of tangible personal property purchased for incorporation into real property. As end users of such tangible personal property, these contractors incur Use Tax liability for such purchases based upon their cost price of the tangible personal property. See 86 Ill. Adm. Code 130.19 and 86 Ill. Adm. Code 130.2075. Therefore, any tangible personal property that a construction contractor purchases that will be permanently affixed to or incorporated into real property in this State will be subject to Use Tax. If such contractors did not pay the Use Tax liability to their suppliers, those contractors must self assess their Use tax liability and pay it directly to the Department. If the contractors have already paid a tax in another state regarding the purchase or use of such property, they will be entitled to a credit against their Illinois Use Tax liability to the extent that they have paid tax that was properly due to another state. See 86 Ill. Adm. Code 150.310.*

*It is important to note that since construction contractors are the end users of the materials that they permanently affix to real estate, their customers incur no Use Tax liability and the construction contractors have no legal authority to collect the Use Tax from their customers. However, many construction contractors pass on the amount of their Use Tax liabilities to customers in the form of higher prices or by including provisions in their contracts that require customer to "reimburse" the construction contractor for his or her tax liability. Please note that this reimbursement cannot be billed to a customer as "sales tax," but can be listed on a bill as a reimbursement of tax. The choice of whether a construction contractor requires a tax reimbursement from the customer or merely raises his or her price is a business decision on the construction contractor's part.*

#### **Additional Statements**

To the best of both the taxpayer and the taxpayer's representative knowledge, the Department has not previously ruled on the same or similar issue for the taxpayer or a predecessor, and the taxpayer nor any representatives previously submitted the same or similar issue to the Department but withdrew it before a letter ruling was issued.

There is no trade secret information contained in this request that need to be removed before public dissemination.

### **Taxpayer Determination**

The company is not a construction contractor because the actual procedures and intent is not to permanently affix the racking system to realty; therefore, the transaction is subject to Retailers' Occupation Tax.

While we do understand that this issue has been continually reviewed by the Department and typically the auditor is in the best position to make this determination; we do not believe the appropriate facts of the company have been aligned with the applicable Illinois position regarding this transaction. For this reason, we respectfully request the Department to review the above information and provide a determination so the company may move forward in compliance with Illinois Law.

If additional information is required or my be of assistance please contact Mr. Z.

Thank you for taking the time to review our request for a Private Letter Ruling to validate our interpretation of the facts.

### **DEPARTMENT'S RESPONSE:**

The Illinois Retailers' Occupation Tax Act imposes a tax upon persons engaged in this State in the business of selling tangible personal property to purchasers for use or consumption. See 86 Ill. Adm. Code 130.101. In Illinois, Use Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. See 86 Ill. Adm. Code 150.101. These taxes comprise what is commonly known as "sales" tax in Illinois. If the purchases occur in Illinois, the purchasers must pay the Use Tax to the retailer at the time of purchase. The retailers are then allowed to retain the amount of Use Tax paid to reimburse themselves for their Retailers' Occupation Tax liability incurred on those sales.

A contract that provides for both the sale and installation of tangible personal property that is permanently affixed or incorporated into a structure is considered a construction contract. See 86 Ill. Adm. Code 130.1940 and 130.2075. The term construction contractor includes general contractors, subcontractors, and specialized contractors such as landscape contractors.

In Illinois, construction contractors are deemed end users of tangible personal property purchased for incorporation into real property. As end users of such tangible personal property, these contractors incur Use Tax liability for such purchases based upon their cost price of the tangible personal property.

Therefore, any tangible personal property that a construction contractor purchases that will be permanently affixed to or incorporated into real property in this State will be subject to Use Tax. If such contractors did not pay the Use Tax liability to their suppliers, those contractors must self assess their Use Tax liability and pay it directly to the Department. If the contractors have already paid a tax in another state regarding the purchase or use of such property, they will be entitled to a credit

against their Illinois Use Tax liability to the extent that they have paid tax that was properly due to another state. See 86 Ill. Adm. Code 150.310.

It is important to note that since construction contractors are the end users of the materials that they permanently affix to real estate, their customers incur no Use Tax liability and the construction contractors have no legal authority to collect the Use Tax from their customers. However, many construction contractors pass on the amount of their Use Tax liabilities to customers in the form of higher prices or by including provisions in their contracts that require customers to "reimburse" the construction contractor for his or her tax liability. Please note that this reimbursement cannot be billed to a customer as "sales tax," but can be listed on a bill as a reimbursement of tax. The choice of whether a construction contractor requires a tax reimbursement from the customer or merely raises his or her price is a business decision on the construction contractor's part.

If subcontractors are utilized and are acting as construction contractors, the transaction between the general contractors and the subcontractors is not a taxable transaction. The subcontractors incur Use Tax liability on any tangible personal property that they purchase for incorporation into real estate. If, however, general contractors make purchases of tangible personal property and then contract to have subcontractors install that tangible personal property, the general contractors incur Use Tax liability on that tangible personal property.

As noted in ST 05-0016 (PLR), for purposes of the Illinois sales tax laws, the Department uses an intention test to determine whether items remain tangible personal property after installation or become part of realty. "If circumstances indicate that the parties obviously intended that the item remain with the realty, we give effect to that intention. If an obvious intent is not apparent, we look to the extent to which the item has been affixed. If the item cannot be removed without damage to the item or to the real estate, that is an indication that the parties intended that the item become part of the realty."

You indicate in your letter that customers may reconfigure the racking systems after a number of years. Your letter does not provide sufficient information for the Department to determine whether the parties intend for the item to remain with the realty. Looking at the manner in which the item is attached to the realty sale, it is apparent there is some damage to the real estate when the systems are reconfigured or removed. Although the fasteners are hammered into the floor, some damage to the floor occurs as a result of this process.

It is the Department's position that the COMPANY is acting as a construction contractor when it sells and installs the storage systems.

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules or in the factual representations recited in this ruling.

I hope this information is helpful. If you have questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws,

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please visit our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard. S. Wolters  
Chairman PLR Committee  
Excise and Sales Tax